



**STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE ENROLLED BILL ANALYSIS**

Date Amended:	Enrolled	Bill No:	SB 1064
Tax:	Sales and Use	Author:	Burton
Board Position:		Related Bills:	

BILL SUMMARY

This bill would amend Section 6902.2 of the Sales and Use Tax Law to clarify the circumstances under which a person may claim a refund with the Board of Equalization (Board), with respect to the manufacturers' income tax credit (MIC) allowed under the Personal Income Tax and the Corporation Tax laws administered by the Franchise Tax Board (FTB).

ANALYSIS

Current Law

Under Section 17053.49 of the Personal Income Tax Law and Section 23649 of the Corporation Tax Law, a 6 percent nonrefundable income tax credit on the cost of equipment is available to manufacturers (MIC). Under these laws, the income tax credit has a carryover feature so that any part of the credit that exceeds the tax liability in the taxable or income tax year for which the credit is claimed may be carried over in future years until the credit is exhausted. Under these provisions, if a taxpayer has no income tax liability during the year to offset the credit, no credit is allowable, regardless of the dollar amount of qualifying property purchased.

Under Section 6902.2 of the Sales and Use Tax Law, those qualified taxpayers eligible for an income tax credit described above, may, in lieu of claiming that income tax credit with the FTB, file a claim for refund with the Board for the tax credit that would have otherwise been allowed under the franchise and income tax laws. The claim for refund may be made for no more than, or no earlier than, the credit that could otherwise be claimed under the franchise and income tax laws.

Proposed Law

This bill would amend Section 6902.2 of the Sales and Use Tax Law to clarify that, a claim for refund filed in lieu of claiming the manufacturers' income tax credit on returns filed with the FTB, may *not* be for an amount in excess of the amount of the credit that could have been used to reduce the "net tax," or "tax," as defined, and that any credit carried over under the franchise and income tax laws may not be refunded until the credit carried over could be applied to reduce the "net tax" or "tax" as defined, and as applicable.

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the Board's formal position.

Background

At its June 25, 2003 hearing, the Members of the Board considered two claims for refund filed pursuant to the provisions of Section 6902.2. The claimants generated a significant dollar amount of income tax credits related to both the manufacturers' income tax credit and other credits related to research and development (R & D). The claimants satisfied their franchise tax liability by using R&D credits, and paid only the alternative minimum tax of \$800.

The claimants then filed a claim for refund under the provisions of Section 6902.2 for the manufacturers' income tax credits that could have been used to offset their income tax had the claimant not credited the income tax with the R & D credits. In a 2-1 vote, the Board approved the refunds at its August 6, 2003 meeting.

COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by the author in an attempt to clarify that under no circumstances may the Board approve a claim for refund filed under Section 6902.2 that exceeds the actual tax liability due to the FTB after the allowance of all applicable credits and other offsets.
2. **Provisions would make pending claims eligible for refund.** The bill would specify that this clarification in law is declaratory of existing law, but is effective for any claims for refund filed on or after August 7, 2003. Essentially this language would authorize the Board, in its discretion, to approve refunds to those taxpayers who have already filed claims for refund on the same grounds. There are currently 28 such claims for refund, totaling \$82.2 million.

COST ESTIMATE

The administrative cost associated with this measure would be absorbable.

REVENUE ESTIMATE

As of the date of this analysis, it is uncertain whether the Board's action on the two claims for refund will serve as a precedent to similar claims not yet presented before the Board. If the Board ultimately decides that its action is precedential, the revenue impact of such a decision would depend on the dollar amount of MIC credits that are available for firms with significant amounts of other credits. According to FTB, it is assumed that corporate taxpayers would amend their tax returns in response to this ruling to minimize their total income/franchise and sale taxes.

FTB reviewed samples of corporate tax returns for the tax years 2000, and 2001. According to FTB, for each corporation, the amount of MIC refund that could be claimed under this ruling was calculated. The amount of MIC refund that could be claimed was calculated as the difference between the amount of MIC that could be claimed if the MIC were claimed before any other credits were claimed and the amount of MIC that could be claimed if the MIC were claimed after the maximum amount of all other credits were claimed. The impact for each individual corporation was then statistically weighted and aggregated to derive an estimate of the total revenue impact for each of the above sampled tax years. The impacts for 2000 and for 2001 were averaged to find the impact for one liability year. It was assumed that there would be about 3 open years for which

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corporate taxpayers could use the approach imbedded in the Board's decision. The estimated total loss for the three years is \$600 million.

As of the date of this analysis, the Board has 28 pending claims for refund totaling \$82.2 million. These claims have not been reviewed by Board staff for accuracy or completeness.

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